

DEPARTMENT OF STATE REVENUE
LETTER OF FINDINGS NUMBER: 02-0340
Sales and Use Tax
For the Years 1999-2000

NOTICE: Under IC 4-22-7-7, this document is required to be published in the Indiana Register and is effective on its date of publication. It shall remain in effect until the date it is superseded or deleted by the publication of a new document in the Indiana Register. The publication of this document will provide the general public with information about the Department's official position concerning a specific issue.

ISSUES

I. Sales and Use Tax- Lump Sum Contracts

Authority: IC 6-8.1-5-1 (b), IC 6-2.5-2-1, IC 6-2.5-3-2 (a), IC 6-2.5-1-1, 45 IAC 2.2-3-9 (e), 45 IAC 2.2-3-7.

The taxpayer protests the assessment of use tax on materials incorporated into its real property.

II. Sales and UseTax- Computer Software

Authority: IC 6-2.5-3-2 (a), Sales and Use Tax Information Bulletin 8, issued February 9, 1990.

The taxpayer protests the assessment of use tax on certain computer software.

III. Sales and Use Tax-Payment of Tax to Another State

Authority: IC 6-2.5-3-2(a), Sales Tax Information Bulletin #31, Section II-B, issued January 31, 1986.

The taxpayer protests the assessment of Indiana use tax on a sign after it had paid Kentucky sales tax.

IV. Tax Administration- Penalty

Authority: IC 6-8.1-10-2.1, 45 IAC 15-11-2 (b).

The taxpayer protests the imposition of the ten percent (10%) negligence penalty.

STATEMENT OF FACTS

The taxpayer is a professional limited liability corporation that built a new surgical facility in Indiana. After an audit, the Indiana Department of Revenue hereinafter referred to as the “department,” assessed additional sales and use tax for the tax period 1999-2000. The taxpayer protested a portion of the assessment and penalty. A hearing was held and this Letter of Findings results.

I. Sales and Use Tax-Lump Sum Contracts

The notice of proposed assessment is prima facie evidence that the department's claim for the unpaid tax is valid. The burden of proving that the proposed assessment is wrong rests with the person against whom the proposed assessment is made. IC 6-8.1-5-1 (b).

Indiana imposes a sales tax on retail sales of tangible personal property in Indiana. IC 6-2.5-2-1. Indiana also imposes a complementary use tax on tangible personal property stored, used, or consumed in Indiana when the sales tax was not paid at the time of purchase. IC 6-2.5-3-2 (a). The department assessed use tax on the taxpayer's use of several items of tangible personal property used in the construction of the taxpayer's facility. The taxpayer protested these assessments.

Regulations clarify the applicability of sales and use tax to construction and improvements to real estate.

45 IAC 2.2-3-9 (e) provides:

Disposition subject to the use tax. With respect to construction materials a contractor acquired tax-free, the contractor is liable for the use tax and must remit such tax (measured on the purchase price) to the Department of revenue when he disposes of such property in the following manner:

- (1) He converts the construction material into realty on land he owns and then sells the improved real estate;
- (2) He utilizes the construction material for his own benefit; or
- (3) Lump sum contract. He converts the construction material into realty on land he does not own pursuant to a contract that includes all elements of cost in the total contract price.

For the purposes of the above Regulation, 45 IAC 2.2-3-7 defines contractor and construction material as follows:

(a) Contractors. For purposes of this regulation [45 IAC 2.2] “contractor” means any person engaged in converting construction material into realty. The term “contractor” refers to general or prime contractors, subcontractors, and specialty contractors, including but not limited to persons engaged in building, cement work, carpentry, plumbing, heating, electrical work, roofing, wrecking, excavating, plastering, tile and road construction.

(b) Construction material. For purposes of the regulation [45 IAC 2.2] “construction material” means any tangible personal property to be used for

incorporation in or improvement of a facility or structure constituting or becoming part of the land on which such facility or structure is situated.

The department assessed use tax on a light signaling system; wire and peripheral equipment used to support the computers, telephones, time clocks, and voice-call system; an illuminated outdoor sign; a fire alarm system; a security system; and venetian blinds. If the department could segregate the actual cost of the tangible personal property from the cost of the labor, the tax was only assessed on the value of the tangible personal property. If the amounts could not be segregated, the department assessed tax on the total value of the invoice. The department considered each of these transactions the sale of tangible personal property subject to either the sales tax or the use tax. The taxpayer protested these assessments contending that they were lump sum contracts for improvements to real estate and the contractors owed the sales tax on the tangible personal property.

Installations including an extensive amount of wiring in the walls of real estate become part of the real estate itself and cannot be removed without significant damage to the real estate. The taxpayer provided substantial evidence that the contracts for the installation of the light signaling system; wire and peripheral equipment used to support the computers, telephones, time clocks, and voice-call system; fire alarm system; and security system were lump sum contracts for the incorporation into and improvement of real estate. Therefore, the contractors are responsible for paying the sales or use tax on the purchases of these items of tangible personal property rather than the taxpayer.

The illuminated outdoor sign and venetian blinds are, however, different. After installation, they retain their character as personal property. They can also be removed doing little damage to the real estate. The department has consistently held that the installation of such items is the sale of tangible personal property. The taxpayer owes the use tax on the amount of the materials in the contract for installation of the sign. The venetian blinds were installed for a single charge with no breakdown of labor and materials. As such, this transaction constitutes a unitary transaction. The use tax is due on the total cost of the unitary transaction for the installation of the venetian blinds. IC 6-2.5-1-1.

FINDING

The taxpayer's protest to the assessments on the venetian blinds and out-door sign is denied. The remainder of the protest is sustained.

II. Sales and Use Tax- Computer Software

DISCUSSION

The department also assessed use tax on the taxpayer's use of certain computer software equipment pursuant to IC 6-2.5-3-2 (a). The taxpayer also protested this assessment. The computer software in question is advertised on the internet to medical offices and surgery centers. It is a specialty, highly customized software with a very broad range of applications. The taxpayer argues that the \$43,000.00 cost of the adaptations evidences the high degree of customization necessary to make the software work properly for the taxpayer.

Sales and Use Tax Information Bulletin 8, issued February 9, 1990, clarifies the application of the sales and use tax to computer software as follows:

(t)ransactions involving computer software are not subject to Indiana Sales or Use tax provided the software is in the form of a custom program specifically designed for the purchaser.

Information Bulletin 8 also states:

Pre-written programs, not specifically designed for one purchaser, developed by the seller for sale or lease on the general market in the form of tangible personal property and sold or leased in the form of tangible personal property are subject to tax irrespective of the fact that the program may require some modification for a purchaser's particular computer. Pre-written or canned computer programs are taxable because the intellectual property contained in the canned program is no different than the intellectual property in a videotape or a textbook.

The computer software in question was not designed specifically for the taxpayer. Rather, it is marketed to medical and surgery facilities across the nation. The department agrees that the software required substantial adaptations before it could be used by the taxpayer. Those adaptations, however, do not change the basic character of the software from taxable canned software to exempt software specifically designed for the taxpayer.

FINDING

The taxpayer's protest is denied.

III. Sales and Use Tax-Payment of Tax to Another State

DISCUSSION

The taxpayer protests the assessment of use tax on the use of an illuminated outdoor sign with pole. Previously in this Letter of Findings, the department denied the taxpayer's protest to the assessment of use tax on the outdoor sign as property installed pursuant to a lump sum contract for improvement to realty. Alternatively, the taxpayer contends that it does not owe the Indiana use tax because it paid the Kentucky sales tax on the sign. Alternatively, the taxpayer argues that it deserves a credit for the Kentucky sales tax paid.

The taxpayer accepted delivery of the sign in Indiana and the sale was completed here. Therefore, the retail transaction is subject to the Indiana sales and use tax rather than the Kentucky sales tax. The use of the items in Indiana is subject to the Indiana use tax pursuant to IC 6-2.5-3-2(a). The Indiana use tax is the tax that is properly due and owing.

The department's position concerning credit for sales taxes paid to other jurisdictions is clearly stated in Sales Tax Information Bulletin #31, Section II-B, issued January 31, 1986 as follows:

A person is entitled to a credit against the Indiana use tax which is equal to the amount of sales tax, purchase tax, or use tax properly and validly paid to another state, territory, or jurisdiction of the United States for the acquisition of a particular item of property. No credit will be allowed if the tax was paid in error to another state and was not due that state.

In this case, the taxpayer owes Indiana use tax on the use of the sign and improperly paid the sales tax to Kentucky. Therefore, the taxpayer does not receive a credit for the sales tax paid to Kentucky.

FINDING

The taxpayer's protest is denied.

IV. Tax Administration- Penalty

The taxpayer protests the imposition of the ten percent (10%) negligence penalty pursuant to IC 6-8.1-10-2.1.

Indiana Regulation 45 IAC 15-11-2 (b) clarifies the standard for the imposition of the negligence penalty as follows:

Negligence, on behalf of a taxpayer is defined as the failure to use such reasonable care, caution, or diligence as would be expected of an ordinary reasonable taxpayer. Negligence would result from a taxpayer's carelessness, thoughtlessness, disregard or inattention to duties placed upon the taxpayer by the Indiana Code or department regulations. Ignorance of the listed tax laws, rules and/or regulations is treated as negligence. Further, failure to reach and follow instructions provided by the department is treated as negligence. Negligence shall be determined on a case by case basis according to the facts and circumstances of each taxpayer.

The taxpayer failed to pay sales tax or self assess use tax on such clearly taxable items as office supplies and consumable surgical supplies. The taxpayer's inattention to its duty to pay these taxes constitutes negligence.

FINDING

The taxpayer's protest is denied.